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In the Supreme Court

OF THE

United States

OCTOBER TERM, 1942

No. 413

PEOPLE OF THE STATE OF CALIFORNIA, on the relation of Charles J. McColgan, as State Franchise Tax Commissioner,

Petitioner,

vs.

JOHN HOWARD BRUCE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI to the United States Circuit Court of Appeals for the Ninth Circuit.

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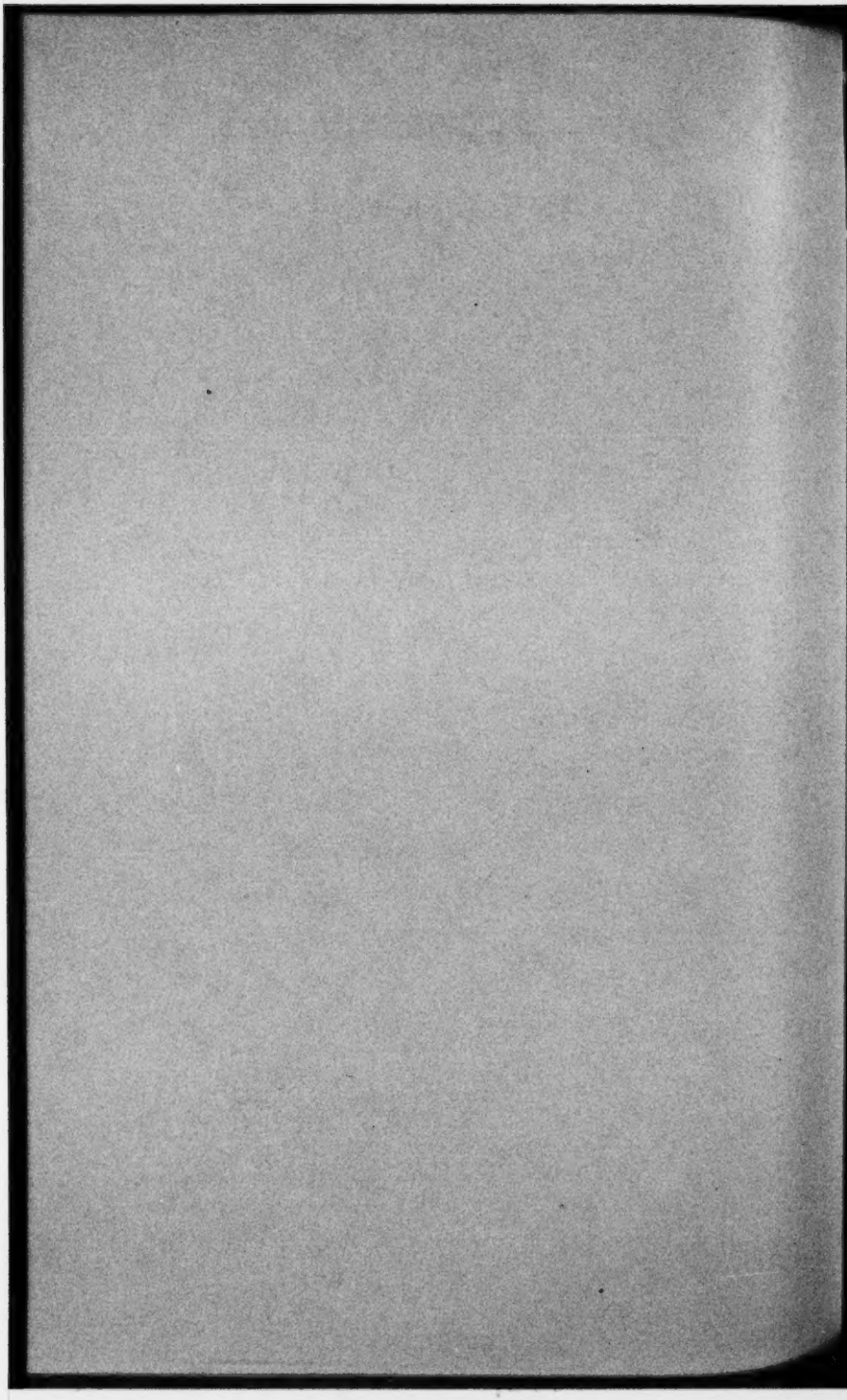

Subject Index

	Page
Opinion Below	2
Jurisdiction	2
Questions Presented	2
Statutes Involved	3
Statement	3
Specification of Errors to be Urged	5
Reasons for Granting the Writ	6
Conclusion	17

Table of Authorities Cited

Cases	Pages
Apicella v. Scala, Irish High Court (Tr. of Record, p. 44)	17
Bradford Electric Light Co. v. Clapper, 286 U. S. 145	9, 11
Broderick v. Rosner, 294 U. S. 629	9, 10, 11, 14
Bullard v. Cisco, 290 U. S. 177	13
Clark v. Williard, 292 U. S. 112	9
Coal Co. v. Blatchford, 11 Wall. (78 U. S.) 172	13
Continental Assurance Co. v. State of Tennessee, 311 U. S. 5	16
Converse v. Hamilton, 224 U. S. 243	9
Faweus Machine Co. v. U. S., 282 U. S. 375	16
Helvering v. Enright Estate, 312 U. S. 636	16
Helvering v. Horst, 311 U. S. 112	5
Hertz v. Knudson, 6 F. (2d) 812	5
In re State, 245 N. W. (Wis.) 844	13
John Hancock Mutual Life v. Yates, 299 U. S. 178	9
Kenney v. Supreme Lodge, 252 U. S. 411	10
Lawrence v. State Tax Commissioner, 286 U. S. 276	16
Massachusetts v. Missouri, 308 U. S. 1	4, 5, 7, 8, 9
Miller v. McColgan, 17 Cal. (2d) 432, 110 Pac. (2d) 419	17
Milwaukee County v. M. E. White Co., 296 U. S. 268	4, 6, 8, 10, 11, 13, 14
Moore v. Mitchell, 281 U. S. 18	11, 14
New York ex rel. Cohn v. Graves, 300 U. S. 308	16
Pfaff v. Commissioner, 312 U. S. 646	16
Scobie v. Wisconsin Tax Commission, 225 Wis. 529, 275 N. W. 531	16
Shaffer v. Carter, 252 U. S. 37	16
St. Louis Union Trust Co. v. State of Missouri, 155 S. W. (2d) (Mo.) 107	8
State of Indiana v. Glover, 155 U. S. 513	13

Pages

United States v. West Virginia, 295 U. S. 463..... 12

West India Oil Co. v. Domenech, 311 U. S. 20..... 15
Wisconsin v. J. C. Penney Co., 311 U. S. 435..... 16

Constitution and Statutes

Constitution:
Article III, Sec. 2, Clause 1.....7, 12, 14
Article IV, Sec. 1..... 9, 11

Judicial Code:
Sec. 24(1) 5, 12, 13, 14
Sec. 24(5) 5, 15
Sec. 240(a) 2

Organic Act of Puerto Rico, Sec. 3, 44 Stats. 1418..... 14

Personal Income Tax Act of the State of California (Calif. Stats. 1935, p. 1090, as amended).....3, 10, 12

Legal Periodicals

California Law Review, Vol. 28, p. 507..... 9, 11

Harvard Law Review, Vol. 49, p. 490..... 6

Illinois Law Review, Vol. 34, p. 610..... 9

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to the United States Circuit Court of Appeals for the Ninth Circuit.

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

Petitioner, People of the State of California, on the relation of Charles J. McColgan, as State Franchise Tax Commissioner, respectfully prays that a writ of certiorari issue to review the judgment of the

United States Circuit Court of Appeals for the Ninth Circuit, entered in the above case on June 26, 1942, reversing the judgment of the United States District Court for the District of Nevada.

OPINION BELOW.

The opinion of the Circuit Court of Appeals is reported in 129 F. (2d) 421. The opinion of the District Court is reported in 37 F. Supp. 811.

JURISDICTION.

The judgment sought to be reviewed was entered on June 26, 1942. The jurisdiction of this court is invoked under section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED.

1. Whether the United States District Court for the District of Nevada has jurisdiction of a suit brought pursuant to state statute by the Franchise Tax Commissioner of the State of California in the name of the people of the State of California against a citizen of the State of Nevada for taxes allegedly due under the California Personal Income Tax Act.

2. Whether the State of California lacked jurisdiction to tax income of the respondent because he was a non-resident of California at the time he actu-

ally received payment although his right to receive payment had vested while he was a resident of California and the property which produced the income was in California.

STATUTES INVOLVED.

The statutes involved will be found in the Appendix.

STATEMENT.

This suit was instituted to collect income taxes allegedly due under the Personal Income Tax Act of the State of California. (Calif. Stats. 1935, p. 1090)

In 1936, respondent, while married, living with his wife, and a resident of California, bought in California from a resident of California an Irish Sweepstakes ticket for the price of $2.50. (R. 2-3) Respondent's name appeared on the counterfoil which was sent to the Sweepstakes officials in Ireland. (R. 3) Soon the drawing occurred in Ireland and respondent's ticket drew a horse which was running in the race. (R. 3) Respondent then sold a half-interest in his ticket to a New York syndicate for $5,000, which sum he subsequently (in April, 1937) reported to the State of California and on which he paid a California income tax. (R. 3) Respondent retained this ticket in his possession at all times. (R. 3) About May 26, 1936, the race was run and the horse drawn by respondent's ticket won first place, entitling the holder or holders of the ticket to the first prize of $150,000. (R.3)

Payment of his winnings was not immediately made to respondent, however, for suit was instituted in the Irish courts by one William Leathe to prevent the payment of the entire proceeds to respondent and to compel payment of half the proceeds to Leathe. (R. 3) This suit was withdrawn by Leathe some time between May 10, 1937 and June 25, 1937, for a settlement of $5,000. (R. 3) Immediately thereafter $75,000 was received by the New York syndicate, and respondent received the other $75,000, less $5,000 used to settle with Leathe and $10,000 for attorneys' fees and expenses. (R. 3) On June 25, 1937 the First National Bank in Reno collected $59,356.66 for respondent and credited that sum to respondent's account less charges. (R. 3)

Respondent and his wife were residents of California when the ticket was purchased and when the race was run. (R. 4) On or about May 10, 1937, they became residents of the State of Nevada. (R. 4)

The California Franchise Tax Commissioner on June 10, 1937 issued a jeopardy assessment against respondent, assessing him with income tax of $4,345.84 on net income of $70,000. (R. 4)

As the assessment was not paid, this action was instituted in the United States District Court for the District of Nevada to recover the unpaid assessment, and respondent was duly served and appeared. (R. 5)

The District Court held that it had jurisdiction, relying upon *Massachusetts v. Missouri,* 308 U.S. 1, *Milwaukee County v. M. E. White Co.,* 296 U.S. 268,

and *Hertz v. Knudson,* 6 F. (2d) 812 (R. 92), but on the merits held that respondent was not liable for the tax, relying upon *Helvering v. Horst,* 311 U.S. 112 (R. 93).

The United States Circuit Court of Appeals for the Ninth Circuit reversed the District Court, holding that the District Court did not have jurisdiction to entertain the suit. (R. 104-111)

SPECIFICATION OF ERRORS TO BE URGED.

The Circuit Court of Appeals for the Ninth Circuit erred:

1. In holding that the District Court did not have jurisdiction of this action.

2. In holding that *Massachusetts v. Missouri,* 308 U.S. 1 does not sustain the jurisdiction of the District Court herein.

3. In holding that the full faith and credit clause of the Constitution did not require the District Court to take jurisdiction of this action.

4. In holding that this is not a suit between citizens of different states within the meaning of section 24(1) of the Judicial Code.

5. In holding that this is not a case arising under a law providing for internal revenue within the meaning of section 24(5) of the Judicial Code.

6. In reversing the judgment of the District Court.

REASONS FOR GRANTING THE WRIT.

1. The writ should be granted in order that there may be a determination of the question whether a federal district court in one state has jurisdiction to entertain a suit based upon the revenue statutes of another state.

The importance of this question to every State of the Union is evident. The States frequently are faced with the very practical problem of how to enforce collection from a tax debtor who has no property within the taxing state and upon whom personal service of process cannot be obtained in the taxing state.

The decision of this court in *Milwaukee County v. M. E. White Co.*, 296 U.S. 268, has been helpful in those instances where it has been possible to obtain personal service of process within the taxing state, followed by a judgment. However, expense, delay, and serious difficulty are involved in obtaining a judgment in the taxing state upon which to sue in another state. And in the instant case it is impossible to obtain personal service of process in California because the person against whom the tax liability is asserted has moved to another state. Cf. 49 *Harv. L. Rev.* 490, 491.

2. The writ should be granted in order that there may be a determination of the question whether the states in seeking to enforce their revenue laws are remediless in the federal courts, despite the evident purpose of the Constitution that a federal forum shall be afforded the states to which they may take their controversies with citizens of other states.

Article III, Section 2, Clause 1, of the Constitution provides that "The judicial Power shall extend * * * to Controversies * * * between a State and Citizens of another State; * * *." Yet, taken together, the decision of this Court in *Massachusetts v. Missouri,* 308 U.S. 1, 18-20, denying a state leave to bring an original action in this Court against citizens of another state, and the decision of the Circuit Court of Appeals in the present suit that the District Court was without jurisdiction, have the net effect of denying the states recourse to any of the federal courts for the purpose of bringing suit to enforce their revenue laws against a citizen of another State.

3. The writ should be granted to set at rest the differences of interpretation which have been placed upon the opinion which this court rendered in *Massachusetts v. Missouri,* 308 U.S. 1, 19, 20.

Although at least two District Courts of the United States, the Attorney-Generals of at least two States and the writers of at least two notes in legal periodicals evidently have understood the opinion to mean that an action based upon its revenue laws may be brought by one state in a federal district court situated in another state, the Circuit Court of Appeals herein holds that the opinion is not susceptible of such interpretation. (R. 108-109). The Circuit Court of Appeals appears to have overlooked the full significance of the final paragraph of the opinion in *Massachusetts v. Missouri,* supra. In that paragraph this Court quoted the Attorney-General of Missouri, evidently with approval, to the effect that "it would seem that Massa-

chusetts should be able to bring a suit against the trustees for the collection of its taxes in either a Missouri state court or in a federal district court in Missouri" and followed the quotation with a reference to the case of *Milwaukee County v. M. E. White Co.*, 296 U.S. 268, 272, a case involving a federal district court.

The decision of this court in *Massachusetts v. Missouri*, supra, was followed by a suit filed by Massachusetts against the trustees in a federal district court in Missouri to collect the claimed taxes. The action was entitled *The Commonwealth of Massachusetts*, Complainant, *v. St. Louis Union Trust Company*, et al., Respondents, and was brought in the District Court for the Eastern Division of the Eastern Judicial District of Missouri. The District Court, as well as the Attorney-General of Massachusetts and the attorneys for the respondents therein, evidently regarded *Massachusetts v. Missouri*, supra, as authority for the point that the District Court had jurisdiction of a suit by Massachusetts against citizens of Missouri for, pursuant to stipulation of the parties, the District Court entered judgment in favor of Massachusetts for $85,050. Reference to this federal district court suit and judgment is made in *St. Louis Union Trust Company v. State of Missouri*, 155 S.W. 2d (Missouri) 107, 108, and 34 *Illinois Law Review* 610, 613.

The District Court for Nevada, in the instant case, also regarded the case of *Massachusetts v. Missouri*, supra, as authority for the view that it had jurisdiction of the action. (R. 92)

The writers of the notes in 34 *Illinois Law Rev.* 610, 612, and in 28 *Calif. Law Rev.* 507, 510, also interpret *Massachusetts v. Missouri,* supra, as suggesting that Massachusetts could bring suit in the federal district courts in Missouri.

In view of the constitutional purpose to afford a federal tribunal in which States may sue citizens of other States, we believe this court would not have denied Massachusetts the right to commence an original proceeding in this Court had it not been of the view that Massachusetts could have access to the federal district courts.

4. The writ should be granted because an important question is involved concerning the effect of Article IV, section 1, of the Constitution upon the jurisdiction of federal district courts.

This Court has held that the full faith and credit clause applies to state statutes. *Bradford Electric Light Co. v. Clapper,* 286 U.S. 145, 155; *Broderick v. Rosner,* 294 U.S. 629, 644; *Converse v. Hamilton,* 224 U.S. 243, 261; *Clark v. Williard,* 292 U.S. 112, 121; *John Hancock Mutual Life v. Yates,* 299 U.S. 178, 183. This Court has held also that because of the provisions of the full faith and credit clause the courts of one state must entertain a suit brought pursuant to the statute of another state even though no such suit is provided for by the statutes of the state in which the suit is brought. *Broderick v. Rosner,* supra. This Court further has held that federal courts are bound equally with state courts to observe the command of the full faith and credit clause. *Bradford Electric*

Light Co. v. Clapper, supra, 155; *Milwaukee County v. M. E. White Co.,* supra. These principles point to the conclusion that the full faith and credit clause requires the federal courts to exercise jurisdiction in this case, independently of the question whether Congress has expressly conferred jurisdiction on the federal district courts to entertain the suit. Congress has established federal district courts with competence and authority to enforce revenue laws and to enforce claims of sovereigns. Under the doctrine of such cases as *Broderick v. Rosner,* supra, 642, and *Kenney v. Supreme Lodge,* 252 U.S. 411, 415, refusal to entertain jurisdiction of this suit is a denial of full faith and credit to the statute of the State of California which provides that the Franchise Tax Commissioner of the State of California may bring an appropriate action in any court of competent jurisdiction in the United States in the name of the people of the State of California to recover the amount of any taxes and interest due under the Personal Income Tax Act of the State of California (The statutory provision, section 28 of the Act, is set forth in the appendix to this Petition).

5. The writ should be granted in order that there may be a determination of a question twice expressly left open by this Court, namely, whether the revenue laws of a state are entitled to full faith and credit in state and federal courts situated in another state.

Assuming that under the doctrine of such cases as *Broderick v. Rosner,* supra, a federal district court, sitting in one state, generally must give full faith and credit to a statute of another state, the additional ques-

tion is involved here as to whether that is true if the statute is a revenue law. See 28 Calif. Law Rev. 507.

In *Milwaukee County v. M. E. White Co.*, 296 U.S. 268, this Court held that a judgment rendered in one state must be given full faith and credit by the federal courts in another state even though the judgment is founded upon a revenue law of the first state. However, in *Milwaukee County v. M. E. White Co.*, supra, p. 275, and in *Moore v. Mitchell*, 281 U. S. 18, 24, this Court expressly left open the question whether a federal court in one state is required to give full faith and credit to the revenue laws of another state. It is a matter of great importance to the States that the question now be determined.

6. The writ should be granted because the opinion of the Circuit Court of Appeals herein is in conflict with the more recent opinions of this Court concerning the nature and effect of Article IV, section 1, of the Constitution.

The Circuit Court of Appeals has taken the position in its opinion that the full faith and credit clause merely establishes a rule of evidence. This is directly contrary to the opinion of this Court in *Broderick v. Rosner*, supra, and *Bradford Electric Light Co. v. Clapper*, supra.

Moreover, the Circuit Court of Appeals reasons in its opinion that if the full faith and credit clause requires the federal district court to entertain this suit then "any attempt, at any time or place, by any person, to enforce the provisions of any state statute or judgment would be, without more, a subject of federal jurisdiction". In so reasoning, the Circuit Court

of Appeals overlooks the well established principle that the judicial power of the federal courts does not extend beyond the limits prescribed by Article III, section 2, of the Constitution. *United States v. West Virginia,* 295 U.S. 463, 470.

7. The writ should be granted to permit the determination of a question concerning the proper application of the diversity of citizenship provision of section 24(1) of the Judicial Code.

Aside from other grounds of jurisdiction herein discussed, it would seem that the jurisdiction of the District Court is sustainable on the basis that this is a suit between citizens of different states. The suit is entitled People of the State of California on the relation of Charles J. McColgan, as State Franchise Tax Commissioner. The State of California undoubtedly has the primary interest in obtaining collection of the tax herein asserted, but the State Franchise Tax Commissioner also has an interest in the outcome of the litigation. Section 28 of the California Personal Income Tax Act authorizes him to bring this action in the name of the people of the State of California, section 32 of that Act imposes on him the duty of enforcing the tax, section 14(c) requires that all taxes due under the Act shall be paid to him and section 21 names him as statutory defendant in actions to contest any disputed tax. Section 31 of the act provides that the Commissioner shall have a certain percentage of the moneys collected, for expenditure in carrying out the provisions of the Act. These provisions of the California Personal Income Tax Act are set forth in the Appendix to this petition.

It would seem, therefore, that for purposes of the diversity of citizenship provision in section 24(1) of the Judicial Code, the Franchise Tax Commissioner may be regarded as a party plaintiff herein. He occupies a position somewhat similar to that occupied by Milwaukee County in *Milwaukee County v. M. E. White Co.,* 296 U.S. 268, wherein jurisdiction of the federal district court was upheld. See *In re State,* 245 N.W. (Wis.) 844, 845. The record in the *Milwaukee County* case shows that the assessment was made by the Tax Commission of the State of Wisconsin and that the county was suing primarily on behalf of the State. Indeed, the question certified to this Court referred to the judgment as being "predicated upon an income tax due from the defendant to the State of Wisconsin". Decisions of this Court involving fiduciaries furnish another instance in which citizenship of persons other than the person primarily interested has been regarded as controlling. *Coal Co. v. Blatchford,* 11 Wall. (78 U.S.) 172; *Bullard v. Cisco,* 290 U.S. 177, 188, 190. The fact that the action is entitled "People of the State of California on the relation of Charles J. McColgan, as State Franchise Tax Commissioner" does not compel a conclusion that the citizenship of the Commissioner may not be regarded. Cf. *State of Indiana v. Glover,* 155 U.S. 513.

The doctrine that in actions against state officers, where a state is the real party in interest, an action against a state officer will be regarded as an action against the state, has no application here for while the Eleventh Amendment prohibits actions against states by citizens of other states there is no constitutional

prohibition against actions by states against citizens of other states. On the contrary, Article III, Section 2, Clause 1, of the Constitution provides that the judicial power of the United States shall extend to such suits. Since no possible infringement of a constitutional prohibition is involved, the rule that substance, not form, governs in the application of constitutional prohibitions has no pertinence here and does not prevent the Franchise Tax Commissioner from being regarded as a party plaintiff for the purposes of the diversity of citizenship provision in section 24(1) of the Judicial Code.

Moore v. Mitchell, supra, may be distinguished from the instant case by the fact that the Indiana statute there involved did not expressly authorize bringing suits in other states, whereas the California statute does. Moreover, *Moore v. Mitchell* appears to be inconsistent with later decisions of this Court in *Milwaukee County v. M. E. White Co.,* supra, and *Broderick v. Rosner,* supra.

8. The writ should be granted in order that there may be a determination of the question whether an action for the collection of state taxes is a case "arising under any law providing for internal revenue" within the meaning of section 24(5) of the Judicial Code.

Congress has not confined the use of the word "internal revenue" to taxes imposed by it. See for example section 3 of the Organic Act of Puerto Rico, 44 Stats. 1418, wherein Congress refers to the territorial tax laws of the Territorial Government as "internal revenue" laws. The pertinent portions of that

Act and of a congressional report regarding it are set forth in a footnote in the report of *West India Oil Co. v. Domenech,* 311 U.S. 20.

The Circuit Court of Appeals did not pass upon the merits of the tax claim but ruled merely on the jurisdiction of the District Court. We recognize that the usual procedure of this Court, if it granted the writ and upheld the jurisdiction of the District Court, would be to remand the case to the Circuit Court of Appeals for a decision upon the merits of the tax claim. We believe the question of jurisdiction of the District Court alone is sufficient to justify the granting of the writ. However, we are aware that the powers of this Court on certiorari are so broad that it may pass upon the merits of the tax claim as well as the jurisdiction of the District Court if it sees fit to do so. Consequently, we shall state briefly the reason why the writ should be granted with reference to the merits of the tax claim:

1. The writ should be granted in order that there may be a determination of the question whether the State of California lacked jurisdiction to tax income of respondent because he was a non-resident of California at the time he actually received payment although his right to receive payment had vested while he was a resident of California and the property which produced the income was in California.

Respondent was a resident of California during 1936 and until May 10, 1937 (R. 2) California had jurisdiction to tax respondent in 1936 and until May

10, 1937, on all his income,, including any from other states or countries. *Lawrence v. State Tax Commissioner,* 286 U.S. 276; *New York ex rel Cohn v. Graves,* 300 U.S. 308. The winnings from the Irish Sweepstakes could properly have been treated by California as accrued income in 1936 when the race was run and the holder of the ticket (respondent) became entitled to the proceeds. The accrual in this case as of the running of the race is clearer and more in accord with recognized accounting concepts of accrual than were the accruals in the cases of *Helvering v. Enright Estate,* 312 U.S. 636, and *Pfaff v. Commissioner,* 312 U.S. 646. Likewise, the case for the accrual of these winnings in 1936 is clearer than the accrual in *Fawcus Machine Co. v. United States,* 282 U.S. 375.

Having had jurisdiction to impose an income tax on respondent's winnings at the time when they first became income, California did not lose jurisdiction to tax merely because it conditioned the imposition of the tax on an event which occurred in another state, *Wisconsin v. J. C. Penney Co.,* 311 U.S. 435, or because the tax was not assessed until respondent had become a resident of another state. *Scobie v. Wisconsin Tax Commission,* 225 Wis. 529, 275 N.W. 531; see also *Continental Assurance Co. v. State of Tennessee,* 311 U.S. 5, and *Wisconsin v. J. C. Penney Co.,* supra.

The jurisdiction of California to impose this tax also is supported by the rule that a state can tax nonresidents on their income derived from within its borders. *Shaffer v. Carter,* 252 U.S. 37. The Sweepstakes ticket was in California when the race was run (R. 3). The ticket, property in California, created income,

because it gave the holder the right to certain proceeds which constituted income. *Apicella et al. v. Scala,* Irish High Court (R. 44, 69, 81, 84). Cf. *Miller v. McColgan,* 17 Cal. (2d) 432, 110 Pac. (2d) 419.

CONCLUSION.

WHEREFORE, it is respectfully submitted that this petition should be granted.

If this Court determines to act favorably upon this petition, we respectfully suggest that it will assist counsel materially in preparing for the argument if this Court, in granting the writ, will indicate whether the writ is limited to the question of the jurisdiction of the District Court or whether it applies also to the merits of the tax claim.

Dated, San Francisco, California,
September 21, 1942.

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(Appendix Follows.)